

## **DEPARTMENT OF STATE REVENUE**

### **Revenue Ruling #99-05 ST**

May 11, 1999

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### **ISSUE**

Sales/Use Tax – "Merchant" Electric Power Generating Station and Wholesale Sales of Electricity

Authority: IC 6-2.5-5-10, IC 6-2.5-4-5, Rule 45 IAC 2.2-4-11

The taxpayer requests the Department to rule on the application of sales/use tax to a "merchant" electric power generating station and to the wholesale sales of electricity. The taxpayer submitted the following statements in relation to this request for Department review.

1. The taxpayer's purchase, storage, use or consumption of all items that would be treated as production plant or power production expenses according to the Uniform System of Accounts for electric utilities, including without limitation all power generation equipment (such as turbines and generators) and consumables (such as natural gas and fuel oil, including such items purchased from an affiliate), will be exempt from Indiana sales and use tax.
2. The taxpayer's wholesale sales of electricity will not be subject to Indiana sales and use tax.
3. The wholesale sales of electricity by the taxpayer's affiliate will not be subject to Indiana sales and use tax.

### **STATEMENT OF FACTS**

The taxpayer is a limited liability company organized and existing under the laws of Delaware and authorized to do business in Indiana. The taxpayer is indirectly owned by

a publicly traded, major energy services company with worldwide operations. The taxpayer was formed for the sole purpose of constructing and operating a new electric power generating station in the Midwest.

The proposed generating station will be capable of generating up to 640 megawatts of electric power, utilizing natural gas as its principal fuel. The facility will be a peaking plant that generates electricity only during times of peak demand. It is anticipated that the generating station's generation of electric power will be seasonal, serving primarily the summer peak demand period.

The generating station will be operated as a "merchant" plant, dedicated to the generation and sale of electricity at wholesale. All sales of electricity will be for resale. The generating station will be interconnected with the transmission system of another energy company and will have no transmission facilities of its own, other than limited interconnection equipment.

It is anticipated that most of the taxpayer's sales of electricity will be made to its power-marketing affiliate for resale. The affiliate will, in turn, resell the electricity to investor-owned utilities, electric cooperatives, municipal electric generators, other power marketers, and other entities for resale. Any other sales of electricity by the taxpayer will be made at wholesale to other entities, including investor-owned and municipal utilities. The taxpayer also expects to obtain its requirements for natural gas and possibly fuel oil from its affiliate.

The taxpayer intends to file an application with the Federal Energy Regulatory Commission (FERC) for a determination that it will be an Exempt Wholesale Generator (EWG). As an EWG, the taxpayer will be prohibited from making retail sales.

The taxpayer also intends to apply to FERC for authorization to sell electricity at wholesale rates subject to FERC's jurisdiction and standards. Specifically, the taxpayer will file a request with FERC for authorization to sell power at market based rates. The price or rate that the taxpayer charges its wholesale electricity customers, however, will not be subject to specific FERC approval. If FERC grants its request, the taxpayer will be a public utility within the meaning of the Federal Power Act and be subject to regulation as such. The taxpayer will be required to comply with certain reporting requirements with respect to (i) its power sale arrangements (e.g., submitting informational filings on the terms of its power sale agreements), (ii) acquisitions of new generation and (iii) its affiliations with entities owning generation or transmission facilities. FERC will impose these reporting requirements so that it can monitor whether the taxpayer continues to satisfy the criteria for generating plants receiving market rate authority (e.g., it lacks transmission and generation market power). In addition, as a Federal Power Act public utility, the taxpayer will be required to seek approvals for certain (a) dispositions or acquisitions of FERC jurisdictional facilities, (b) corporate reorganizations, and (c) financing transactions. As an EWG, the taxpayer will also be required to report to FERC certain material changes in its operations so that FERC can monitor whether it still qualifies for EWG status.

The taxpayer also filed a petition with the Indiana Utility Regulatory Commission (the IURC) to determine its status as a utility under the Indiana Public Service Commission Act. The IURC entered an order on the taxpayer's petition on April 7, 1999 ruling that the taxpayer is a public utility within the meaning of the Indiana Public Service Commission Act and, thus, subject to regulation by the IURC, but, pursuant to IC 8-1-2.5-5, the IURC declined to exercise its regulatory authority over the taxpayer.

The taxpayer agrees and plans for its accounting for the generating station to conform with the requirements of the Uniform System of Accounts prescribed by FERC and the IURC for electric utilities.

### **STATEMENT #1 – DISCUSSION**

IC 6-2.5-5-10 states:

Transactions involving tangible personal property are exempt from the state gross retail tax, if:

- (1) the property is classified as production plant or power production expenses, according to the uniform system of accounts which was adopted and prescribed for the utility by the Indiana utility regulatory commission; and
- (2) the person acquiring the property is:
  - (A) a public utility that furnishes or sells electric energy, steam, or steam heat in a retail transaction described in IC 6-2.5-4-5. . .

IC 6-2.5-4-5 states:

- (b) A . . . person engaged as a public utility is a retail merchant making a retail transaction when the . . . person furnishes or sells electrical energy, natural or artificial gas, water, steam, or steam heating service to a person for commercial or domestic consumption.

Regulation 45 IAC 2.2-4-11 defines a public utility for sales tax purposes as follows:

- (d) the term "public utilities" as used in this regulation [45 IAC 2.2] means any organization which is engaged in the furnishing or selling of electricity . . . and having the right of eminent domain or subject to government regulation in connection with the furnishing of public utility services. . .

The IURC has ruled that the taxpayer is a "public utility" pursuant to IC 8-1 thus making the taxpayer "subject to" IURC regulation and, in addition, the taxpayer will be subject to regulation as a public utility by FERC under the Federal Power Act, therefore, the taxpayer is a "public utility" for purposes of both IC 6-2.5-4-5

and IC 6-2.5-5-10 and within the meaning of 45 IAC 2.2-4-11. As a "public utility" all of the taxpayer's machinery, equipment and other tangible personal property that is treated as production plant or power production expenses according to the Uniform System of Accounts for electric utilities are exempt from Indiana sales/use tax.

### **STATEMENT #1 – RULING**

The taxpayer's purchase, storage, use or consumption of all items that would be treated as production plant or power production expenses according to the Uniform System of Accounts for electric utilities, including without limitation all power generation equipment (such as turbines and generators) and consumables (such as natural gas and fuel oil, including such items purchased from an affiliate), will be exempt from Indiana sales and use tax.

### **STATEMENT #2 - DISCUSSION**

IC 6-2.5-4-5(b) provides that sales of electrical energy by a public utility constitute retail transactions subject to sales tax; however, IC 6-2.5-4-5(c)(2) exempts sales to "another public utility".

(c) Notwithstanding subsection (b), a . . . person engaged as a public utility is not a retail merchant making a retail transaction when:

. . .

(2)The . . . person sells the services or commodities listed in subsection (b) to another public utility or power subsidiary . . . ;

For the purpose of the imposition of sales tax under IC 6-2.5-4-5(c) the Department has determined that "a person engaged as a public utility" includes anyone selling utility services. The "sales for resale" (wholesale sales) by the taxpayer, therefore, are exempt from sales tax as the purchasers of the electricity, also, meet the definition of "public utility".

### **STATEMENT #2 – RULING**

The taxpayer's wholesale sales of electricity will not be subject to Indiana sales and use tax.

### **STATEMENT #3 – DISCUSSION**

As discussed in above "Statement #2", the Department has determined that for the purpose of the imposition of sales tax under IC 6-2.5-4-5(c) "a person engaged as a public utility" includes anyone selling utility services. Here then, both the taxpayer's

affiliate and the purchasers of the electricity sold by the taxpayer's affiliate are "public utilities", hence, the sales of electricity by the taxpayer's affiliate are not subject to sales tax.

### **STATEMENT #3 – RULING**

The wholesale sales of electricity by the taxpayer's affiliate will not be subject to Indiana sales and use tax.

### **CAVEAT**

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in a statute, a regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

Department of State Revenue